

Report on Examination
of the
Physicians Insurance Exchange
As of
December 31, 1995

Affidavit of the Chief Examiner

I HEREBY CERTIFY that I have read and reviewed the attached Report on Examination of **Physicians Insurance Exchange** dated November 15, 1996 which shows the financial condition and affairs of the Exchange as of December 31, 1995.

Jacqueline L. Gardner, CFE, FLMI
Chief Examiner

Date

Physicians Insurance Exchange

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Seattle, Washington
January 30, 1997

The Honorable Glenn Pomeroy
NAIC Chairman, Financial Condition (Ex-4) Subcommittee
North Dakota Department of Insurance
600 E. Boulevard
Bismarck, ND 58505-0320

The Honorable Marianne K. Burke
NAIC Secretary, Western Zone
Department of Commerce & Economic Dev.
PO Box 110805
Juneau, AK 99811-0805

The Honorable Deborah Senn
Insurance Commissioner, State of Washington
PO Box 40255
Olympia, WA 98504-0255

Dear Commissioners:

Pursuant to your instructions, and in compliance with the laws of the State of Washington, an examination was made of the corporate affairs and financial records of:

Physicians Insurance Exchange

hereinafter referred to as the "Exchange", at its home office located at 1730 Minor Avenue, Suite 1800, Seattle, Washington 98101. This report of examination is respectfully submitted showing the financial condition of the Exchange as of December 31, 1995.

Scope of Examination

The previous examination of the Exchange was performed as of December 31, 1990. The current examination covers the period from January 1, 1991 through December 31, 1995, and was conducted by insurance examiners from the State of Washington. The examination was conducted in accordance with the examination procedures recommended in the NAIC Examiners' Handbook Volume I, and Title 48, Revised Code of Washington.

Instructions

The Company is instructed to comply with the following:

Pursuant to RCW 48.07.130(1), no officer or director shall be pecuniarily interested in any capacity in investments of the Company. The Company has an investment interest in United Physicians of Washington (UPW). Several members of the Board of Directors have personal investments in UPW, and most physician directors have contracts with UPW. The Company is instructed to take all actions necessary to bring it into compliance with RCW 48.07.130 (1). (Conflict of Interest)

Comments and Recommendations

1. EDP Systems Controls

The Exchange has not formally documented its System Development Life Methodology. The examiners noted that procedures have been established but were not documented. It is recommended the Company develop a manual for this system.

2. Accounting Procedures and Policy Manual

The Exchange does not maintain an accounting procedures or policy manual. We recommend that the Exchange develop a procedures manual. The Company's adoption of this recommendation will facilitate review of controls and training of new employees.

3. Tax Allocation Agreement

The Exchange's tax allocation agreement with the affiliates dated October 30, 1989 should be updated to include new companies added to the group, such as Association Insurance Services, Inc. and PHYSIS Corporation.

4. Bonds

We recommend that the Custodial Agreement with U.S. Bank of Washington for the Scudder, Stevens & Clark account and the WSPIA account be updated to include provisions for indemnifying the Company for the loss of securities, as recommended by the NAIC, and to reflect the current names of the parties.

5. Common Stocks

We recommend that the stock certificate of Association Insurance Services, Inc. be updated to identify Physicians Insurance Exchange as the owner of the twenty thousand (20,000) shares of stocks outstanding as required by RCW 48.12.010.

We also recommend that the Company accurately report the number of shares owned of Association Insurance Services, Inc., as twenty thousand (20,000) instead of one (1) as reported in Schedule D-Part 2 Section 2 of the Annual Statement.

We also recommend that the Company report the correct number of shares owned of PHYSIS Corporation as three hundred thousand (300,000) instead of three hundred (300) shares as reported in Schedule D-Part 2-Section 2 of the Annual Statement.

History and Capitalization

Physicians Insurance Exchange was organized under the laws of the State of Washington under the name Washington State Physicians Insurance Exchange (WSPIE) on December 15, 1981. From its inception in 1981 until 1993, the Exchange used the name WSPIE, at which time it began to use Physicians Insurance Exchange.

The Exchange was organized as a “reciprocal insurer” pursuant to Chapter 48.10 RCW for the purpose of insuring its members against loss, liability, or damage arising out of the practice of medicine or osteopathy. In addition to professional liability insurance, the Exchange is also authorized to write business owners policies, and coverage for comprehensive general liability, directors and officers, and hospital liability coverage. The Exchange is an unincorporated aggregation of subscribers operating individually and collectively through an attorney-in-fact to provide insurance among themselves.

Surplus requirements for the Exchange were funded through a \$2,400,000 loan to the Washington State Physicians Insurance Association (the Association) from Peoples National Bank (now US Bank of Washington) and a \$240,000 loan from its sponsor, the Washington State Medical Association (WSMA). The funds were transferred by the Association to the Exchange with a Surplus Contribution Certificate. The loans were guaranteed through Subordinated Surplus Loan Agreements provided by each member physician as a condition of membership.

Upon approval by the Subscribers Advisory Council under a plan of refinancing, both of these loans

were paid in January of 1984 by the Association and the loan guarantees were returned to the subscribers. The refinancing plan provides that, the Association, as the attorney-in-fact, was authorized to hold premiums for up to 90 days prior to remitting premiums to the Exchange. Funds held by the Association pursuant to the revised collection arrangement were utilized to pay off the Association's note payable to People's National Bank of Washington.

The Surplus Contribution Certificates issued by the Exchange to the Association remained in place until repayment was recorded on March 31, 1992. The repayment was made in accordance with the letter from the Exchange, dated May 1, 1992, to the Office of the Insurance Commissioner.

The Exchange is overseen by a subscribers advisory committee which is called the Subscribers Council (SC). The subscribers elect two representatives from each of the nine congressional districts of Washington who may serve a maximum of nine years. The Council is governed by the Rules of the Exchange and is responsible for oversight of the finances of the Exchange, and the selection of the Attorney-In-Fact.

Affiliated Companies

Washington State Physicians Insurance Association:

Washington State Physicians Insurance Association (WSPIA) manages the business operation of the Exchange as its appointed Attorney-In-Fact. WSPIA has served as the Attorney-In-Fact since the inception of the Company in 1981. Its powers, rights and duties are set out in the Power of Attorney Agreement which is subject to yearly renewal by the Exchange. WSPIA has responsibility for establishing premium rates, the production, underwriting and servicing of insurance, reinsurance, investment, financial audits, and claim handling for members of the Exchange. The business and affairs of the Association is vested in a Board of Directors, the number of which shall not be less than the minimum required by law nor more than eighteen.

Washington State Medical Association (WSMA) is the sole shareholder of the WSPIA, and its Board of Trustees elects members of the WSPIA Board of Directors. Ten physician members and two non-physician members comprise the Board. The elected non-physician members may not be employed in the insurance industry or be engaged in the practice of law. In addition, the WSPIA President and Chief Executive Officer and the Executive Director of WSMA are voting members of WSPIA's Board.

WSPIA bylaws and the Rules of the Exchange call for six Joint Standing Committees. These are the Audit, Claims, Investment, Nominating, Risk Management and Underwriting/Marketing Committees. The Committees are made up of members of the WSPIA Board, the Subscribers Council, and the appropriate WSPIA senior staff. The WSPIA Bylaws also provide for an Executive Committee consisting of the Chairman and Vice Chairman of the Board, three additional Board members, and the President and Chief Executive Officer.

Northwest Dentist Insurance Company (NORDIC):

Northwest Dentist Insurance Company (NORDIC) was created in 1989 as a wholly owned subsidiary of the Exchange to insure dentists in the state of Washington. NORDIC is a for-profit domestic insurance company. NORDIC is endorsed by the Washington State Dental Association (WSDA).

NORDIC has a Board of Directors composed of one member of the WSPIA Board of Directors, two members from the Subscribers Council, three members from the dentist community (WSDA) and the President and Chief Executive Officers of WSPIA. NORDIC contracts with WSPIA for all insurance services such as marketing, underwriting, risk management and claims handling. NORDIC has no employees.

Association Insurance Services, Inc. (AIS):

Association Insurance Services, Inc., (AIS) does business as Physicians Insurance Agency and was established as a for-profit subsidiary of WSPIA to offer additional lines of insurance to Physicians Insurance Exchange subscribers. Physicians Insurance Exchange owns all of the stock, and AIS has its own Board of Directors. The current focus of AIS is to write life insurance and group and individual disability income insurance for physicians. WSPIA staff conducts the business of AIS under a management agreement.

PHYSIS Corporation:

PHYSIS Corporation is a wholly-owned financial service subsidiary of Physicians Insurance Exchange. PHYSIS is registered with the federal Securities and Exchange Commission and with the Washington State Securities Department as an investment advisor. Although the organization was created specifically to address the changing financial needs of physicians and dentists insured by the Exchange and Northwest Dentist Insurance Company, its services are also offered to non-insured groups and individuals. PHYSIS provides the following consulting services to qualified retirement plans and individual investors: retirement plan evaluation, use of prototype retirement plan documents, assistance in establishing investment goals and guidelines, investment searches, performance monitoring and evaluation, participant educational programs, and personalized estate planning. PHYSIS receives compensation from its clients on a fee-for-service basis.

Management and Control

The business affairs of the Exchange are conducted under the direction of experienced insurance executives and the Board of Directors of Washington State Physicians Insurance Association, acting as attorney-in-fact, and its Subscribers' Council.

Pursuant to RCW 48.10.080(3), the Subscribers and the Attorney in Fact comprise a reciprocal insurer and a single entity for purposes of RCW 48.14 (fees and taxes) as to all operations under its certificate of authority. The subscribers elect a subscribers' council and delegate to it full power and authority to act on behalf of the Exchange. The subscribers council for all purposes constitutes the Subscribers' Advisory Committee that supervises the finances, operations, and business affairs of the Exchange to the extent necessary to assure conformity with the Power of Attorney between the Exchange and the Attorney-In-Fact (the "Association").

The attorney-in-fact (The Washington State Physicians Insurance Association, Inc.) is a wholly owned subsidiary of the Washington State Medical Association. The Association's sole purpose, as stated in Article III of its Articles of Incorporation, is to act as attorney-in-fact for the Washington Physicians Insurance Exchange.

Washington State Physicians Insurance Association (Attorney-In-Fact)

Board of Directors:

Board of Directors of the corporation, who are physicians, must be in practice in the State of Washington, cannot be a current member of the Subscribers Council, shall be a member of the Washington State Medical Association, or a current President or President-Elect, and must have professional liability insurance issued by Physician Insurance Exchange. For the entire term of service on the Board of Directors of the Corporation, each director who is eligible to vote, other than the President and Chief Executive Officer of the Washington Physician Insurance Association, shall not be actively engaged in the insurance industry and shall not be an attorney-at-law in active practice, as defined by the Joint Nominating Committee.

Directors serving the Association as at December 31, 1995 were as follows:

<u>Name</u>	<u>Affiliation</u>	<u>Director Since</u>
Rick L. Johnson, MD	Seattle Physician Chairman	Nov. 1987
J. Thomas Rulon, MD	Spokane Physician Vice Chairman	Nov. 1990
Thomas J. Curry	Executive Director WSMA	May 1989
Patrick M. Fahey	Chairman & CEO Pacific Northwest Bank	Nov. 1989
Lon M. Hatfield, MD	Colville, Physician	Jan. 1995
Robert C. Jeffery, MD	Edmonds, Physician	Nov. 1993
Ralph A. Johnson, MD	Tacoma, Physician	Nov. 1988
Thomas A. Kerns, MD	Yakima, Physician	Nov. 1986
James T. Kilduff, MD	Bremerton, Physician	Nov. 1992
Dennis J. Kvidera, MD	Seattle, Physician	Nov. 1985
G. Thomas Miller, MD	Spokane, Physician	Nov. 1985
Nola Mae Moore, MD	Seattle, Physician	Nov. 1990
Richard S. L. Roddis, JD	Bellevue, WA	Nov. 1989
Richard W. Seaman, MD	Olympia Physician	Jan. 1995
Alfred M. Yamashiro	President & CEO	Mar. 1988

Officers:

The following officers served the Exchange as of December 31, 1995:

Name	Position/Designation
Alfred M. Yamashiro	President and Chief Executive Officer
Richard E. Brown	Senior Vice President/Finance & Administration and Chief Financial Officer
Thomas A. Fine	Senior Vice President /Underwriting & Marketing
D. Chip Burrows	Vice President/Claims
Niles A. Cole	Vice President /Controller
Paul A. Buckner	Vice President /Regional Office
Gary L. Morse	Vice President/General Counsel
Vince A. Rota	Vice President/Hospitals
Thomas L. Myers	Vice President/Marketing
Jerry E. Du Puis	Vice President/NORDIC Operation
Thomas E. Kirchmeier	Vice President/Risk Management
John M. Coons	Vice President/Treasurer

Name	Position/Designation
John R. Karlen	Vice President/Underwriting
Patricia C. Berger	Associate Vice President/Claims Litigation
Judith J. Mix	Associate Vice President/Corporate Secretary
Pamela B. Tinsley	Associate Vice President/Underwriting Services

Corporate Records

The WSPIA Board of Directors, as the designated attorney-in-fact of the Exchange, meet quarterly to discuss the business of the Exchange. Complete minutes of all the meetings of the Board and each committee were recorded and kept by the Associate Vice President Secretary. The examination of the minutes of the Board of Directors and Committee meetings disclosed that the Company is in compliance with the applicable statutes as relates to corporate records.

Internal Security

The Exchange has established policies and procedures to protect its assets and business. These include conflict of interest policies, a State AntiFraud Plan, a business recovery plan, various insurance and umbrella policies, and having an independent audit. Additionally, the Company has a disaster recovery plan.

The Company owns stock in Unified Physicians of Washington (UPW). Several members of the Company's Board of Directors have personal investments and interests in UPW. RCW 48.07.130 describes conditions and restrictions of pecuniary interests of officers or directors. Physicians Insurance Exchange should make every effort to be in compliance with this Code section.

Territory and Plan of Operations

The Exchange has authority to write business in Alaska, Idaho, Montana, Oregon, and Washington. The Exchange markets its policies directly to the subscribers.

Growth of the Company

The following data was taken from the Company's annual statements.

<u>Year</u>	<u>Direct Premiums Written</u>	<u>Admitted Assets</u>	<u>Policyholders Surplus</u>
1991	\$50,753,950	\$165,089,540	\$27,825,090
1992	\$48,049,170	\$191,268,740	\$34,255,280
1993	\$50,462,880	\$210,409,210	\$41,274,140
1994	\$48,129,300	\$221,422,610	\$46,765,050
1995	\$45,959,900	\$218,848,760	\$50,182,482

Reinsurance

The Exchange has the following reinsurance in effect as of December 31, 1995:

Reinsurance Assumed:

Physicians Insurance Exchange assumes business from Northwest Dentist Insurance Company (NORDIC), a subsidiary company.

Reinsurance Ceded:

The Exchange has entered into reinsurance agreements with authorized reinsurers for the following protection:

<u>Type of Contract</u>	<u>Retention Level</u>	<u>Reinsurance Limits</u>
First Excess of Loss	\$750,000	\$3,000,000 Ultimate Net Loss Each and Every Loss
Combined Risk and Contingent Excess Loss	\$2,000,000	\$3,000,000 Ultimate Net Loss Each and Every Loss Each Insured
Second Contingent Excess of Loss	\$6,000,000	\$9,000,000 Ultimate Net Loss Each and Every Loss
70% Quota Share, BOP	30% of Each and Every Policy	70% of Variance Level
75% Quota Share, Non-Standard Physicians	25% of \$5 million in Losses	75% of \$5,000,000

All reinsurance agreements in effect as of December 31, 1995 were reviewed. The Exchange has

entered into reinsurance agreements with authorized companies or has made necessary provisions for unauthorized reinsurers. Every agreement included the required insolvency clauses.

Recoverables from reinsurers were \$17,892 on paid losses, \$8,741,000 on unpaid losses and \$15,228,000 on incurred but not reported losses as of December 31, 1995.

Accounts and Records

The accounts and records of the Exchange are maintained on electronic data processing equipment consisting of a mainframe computer, numerous IBM compatible personal computers and PS/2 computer terminals. The Exchange developed the following software packages in house: policy master files, billing and premium accounting, maintenance of the claim files, and loss and loss adjustment reserves. The Exchange utilizes commercial software packages to maintain the General Ledger and Accounts Payable System.

The system software, application programs, libraries and data files are stored in the computer room which is safeguarded and available only to the information system (IS) personnel.

The Company does not have documentation for the following applications: systems, programs, operating procedures, key-entry procedures, control unit balancing procedures and output distributions instructions. The examiners recommend that the Company prepare a Documentation Standard Manual for every application in use. Having a Documentation Standard Manual in place will also enhance the Exchange's newly established AntiFraud plan.

The Company does not have an accounting and procedures manual. These manuals are fundamental tools for evaluating operating procedures and training new employees.

The Company's intercompany tax allocation agreement does not include all participants, such as new affiliates, Association Insurance Services, Inc., and PHYSIS Corporation.

The Company's custodial agreement with U.S. Bank does not include a provision for indemnification of loss of securities, as recommended by the NAIC.

The Company's Annual Statement included reporting errors in the number of shares owned in affiliated companies, Association Insurance Services, Inc., and PHYSIS Corporation.

Subsequent Events

In the August 1995, executive meeting of the Board of Directors, the President was given authority to negotiate and enter into agreements, subject to the approval of the Board of Directors and the Subscribers Council. The agreements with other physician controlled medical professional liability insurers to consolidate and integrate by merger, common ownership, consortium, or joint venturing of functions, have the objectives of,

1. Creating adequate underwriting capacity to compete in emerging markets for professional liability insurance and related lines of insurance.
2. Controlling expenses by achieving greater economy of scale,
3. Developing ancillary lines of business and enhancing market access,
4. Expanding the geographic area of accessible markets, and
5. Retaining physician control of the venture to the greatest extent possible.

This event could occur in the current year or in the years ahead. The financial impact of the restructuring plan to the Exchange was not determined during this examination.

Financial Statements

PHYSICIANS INSURANCE EXCHANGE
COMPARATIVE BALANCE SHEET
AS OF DECEMBER 31,

	<u>1995</u>	<u>1994</u>
<u>ASSETS</u>		
Bonds	\$ 194,937,408	\$ 153,021,765
Stocks:		
Preferred stocks	5,991,325	8,570,824
Common stocks	4,587,462	4,172,710
Cash on hand and on deposit	616,438	101,051
Short-term investments	7,638,227	47,598,959
Agents' balances or uncollected premiums:		
Premiums and agents' balances in course of collection	618,961	(1,059,630)
Reinsurance recoverables on loss and loss adjustment expense payments	17,892	61,413
Federal income tax recoverable	505,668	2,333,082
Electronic data processing equipment	249,717	273,314
Interest, dividends and real estate income due and accrued	2,753,967	2,464,109
Receivable from parent, subsidiaries and affiliates	20,786	37,236
Aggregate write-ins for other than invested assets	910,915	3,847,778
Total Assets	\$ 218,848,766	\$ 221,422,611
<u>LIABILITIES</u>		
Losses	\$ 116,947,529	\$ 125,242,971
Reinsurance payable on paid loss and loss adjustment expenses	5,230	5,369
Loss adjustment expenses	42,565,569	38,239,437
Other expenses	1,390,463	1,187,485
Taxes, licenses and fees (excluding federal and foreign income taxes)	13,529	28,980
Unearned premiums	417,992	840,046
Dividends declared and unpaid:		
Policyholders	2,999,491	4,198,262
Provision for reinsurance	107,000	575,000
Aggregate write-ins for liabilities	4,219,647	5,340,007
Total Liabilities	168,666,450	175,657,557
<u>SURPLUS AND OTHER FUNDS</u>		
Gross paid in and contributed surplus	588,276	1,189,951
Unassigned funds (surplus)	49,594,040	44,575,103
Total Surplus as Regards Policyholders	50,182,316	45,765,054
Total Liabilities, Surplus and Other Funds	\$ 218,848,766	\$ 221,422,611

No examination adjustments were made.

PHYSICIANS INSURANCE EXCHANGE
COMPARATIVE STATEMENT OF INCOME
FOR THE YEARS ENDED DECEMBER 31,

	<u>1995</u>	<u>1994</u>
<u>UNDERWRITING INCOME</u>		
Premiums earned	\$ 36,398,730	\$ 36,020,300
DEDUCTIONS		
Losses Incurred	21,419,218	24,304,640
Loss expenses incurred	15,916,807	9,077,386
Other underwriting expenses incurred	4,723,981	4,680,017
Total Underwriting Deductions	<u>42,060,006</u>	<u>38,062,043</u>
Net Underwriting Gain or (loss)	(5,661,276)	(2,041,743)
<u>INVESTMENT INCOME</u>		
Net investment income earned	12,139,287	10,154,559
Net realized capital gains or (losses)	875,109	551,227
Net Investment Gain or (Loss)	<u>13,014,396</u>	<u>10,705,786</u>
<u>OTHER INCOME</u>		
Net gain or (loss) from agents' or premium balances charged off	(7,200)	(779)
Finance and service charges not included in premiums	494,158	594,036
Aggregate write-ins for miscellaneous income	1,478,175	1,022,514
Total Other Income	<u>1,965,133</u>	<u>1,615,771</u>
Net income before dividends to policyholders and before federal and foreign income taxes	9,318,253	10,279,814
Dividends to policyholders	<u>2,895,445</u>	<u>4,120,652</u>
Net income, after dividends to policyholders but before federal and foreign income taxes	6,422,808	6,159,162
Federal and foreign income taxes incurred	1,009,327	978,314
Net Income	<u>\$ 5,413,481</u>	<u>\$ 5,180,848</u>

No examination adjustments were made.

PHYSICIANS INSURANCE EXCHANGE
COMPARATIVE CAPITAL AND SURPLUS ACCOUNT
AS OF DECEMBER 31,

	1995	1994	1993	1992	1991
CAPITAL AND SURPLUS ACCOUNT					
Surplus as regards policyholders, December 31 previous year	\$ 45,765,054	\$ 41,274,142	\$ 34,455,282	\$ 27,825,095	\$ 21,379,857
GAINS AND (LOSSES) IN SURPLUS					
Net income	5,413,481	5,180,848	7,180,307	9,839,012	6,308,020
Net unrealized capital gains or (losses)	(682,608)	43,425	477,484	87,253	248,835
Change in non-admitted assets	(179,936)	(53,536)	33,874	(82,200)	181,550
Change in provision for reinsurance	468,000	(87,000)	(272,880)	63,222	(278,167)
Aggregate write-ins for gains and losses in surplus	(601,675)	(592,825)	(599,925)	(3,277,100)	(15,000)
Changes in Surplus as Regards Policyholders for the Year	4,417,262	4,490,912	6,818,860	6,630,187	6,445,238
Surplus as Regards Policyholders, December 31 Current Year	\$ 50,182,316	\$ 45,765,054	\$ 41,274,142	\$ 34,455,282	\$ 27,825,095

Notes to the Financial Statements:

1. Basis of Presentation:

The accompanying financial statement has been prepared in conformity with accounting practices and procedures prescribed by the National Association of Insurance Commissioners and the State of Washington.

2. Basis of Valuation of Invested Assets:

- a. Assets are valued as follows: Bonds not backed by loans are reported at amortized cost using the effective yield (scientific) method; loan backed bonds and structured securities are reported at cost using the pro rata method; preferred stock at cost; common stock at market except that investments in stocks of uncombined subsidiaries are reported on the equity basis.
- b. Depreciation is calculated using the ACRS and the modified ACRS methods.
- c. Prepayment assumptions for loan backed bonds and structured securities were obtained from broker dealer survey values or internal estimates.

3. Federal Income Tax Allocation:

- a. The Exchange's Federal Income Tax Return is consolidated with the subsidiaries, Northwest Dentist Insurance Company, Association Insurance Services, and PHYSIS Corporation. The method of allocation is subject to written agreement, approved by the Board of Directors. Allocation is based upon separate return calculations with current credit for net losses.
- b. The amount of Federal Income Taxes incurred and available for recoupment in the event of future net losses is: Current Year \$971,928, first preceding year \$3,558,136, and second preceding year \$5,949,234.
- c. No net losses are available to be carried forward to future years.

4. Information Concerning Parent, Subsidiaries and Affiliates:

- a. The Exchange is a reciprocal. Substantially all activities of the Exchange are conducted by its attorney-in-fact, Washington Physicians Insurance Association, Inc., a wholly-owned subsidiary of the Washington Medical Association. All costs incurred by the Association are reimbursed by the Exchange under the terms of the attorney-in-fact agreement, and are included in the Underwriting and Expenses Exhibit under their appropriate classifications.

5. Deferred Compensation and Retirement Plans:

- a. Employee Retirement Plan: The Company has a Defined Contribution noncontributory pension plan covering all employees. The Company contributes 10% of each employee's compensation each year.
- b. Deferred Compensation Plan: The Company has a contributory 401(K) salary reduction plan for which all employees are eligible. Costs are funded as they accrue.
- c. Post-Retirement Benefit Plan: The Company does not have any post-retirement benefit plans.

6. Interest, Dividends and Real Estate Income Due and Accrued:

The examination disclosed that an interest payment of \$142,560 was received as of September 30, 1996, and the interest accrual was not adjusted to reflect the interest receipt, causing the accrual to be overstated by the same amount. The discrepancy has been brought to the attention of the Controller.

7. Unpaid Losses and Loss Adjustment Expenses:

The reserves carried by the Company for these liabilities were \$116,947,529 and \$42,565,569, respectively, as of December 31, 1995.

The Company furnished the Commissioner's Office with loss and loss adjustment expense development data by accident year and policy year as of November 30, 1995. The data was analyzed by the casualty actuary of the Commissioner's Office. The actuary obtained additional information by interviewing several Company employees. He also reviewed reports prepared for the Company by its consulting actuarial firm, Tillinghast.

Based on the actuary's analysis, the Company's reserves for unpaid losses and unpaid loss adjustment expenses are within a reasonable range. Therefore, the reserves are accepted for this report as shown on the 1995 Annual Statement.

Acknowledgment

The examiners hereby express their gratitude and thanks for the cooperation extended to them by the officers and employees of the Exchange during the examination.

In addition, Peter M. Mendoza, CFE, CIE, Examiner In Charge, John Jacobson, AFE, Kendy Ovbiebo, Insurance Examiners, and Lee Barclay, Property and Casualty Actuary for the Office of the Washington State Insurance Commissioner, participated in the examination and the preparation of the report of examination.

AFFIDAVIT OF EXAMINER IN CHARGE

State of Washington)
) ss
County of King)

Peter M. Mendoza, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

He attests that the examination of Physicians Insurance Exchange was performed in a manner consistent with the standards and procedures required or prescribed by the Washington Office of the Insurance Commissioner and the National Association of Insurance Commissioners (NAIC).

Peter M. Mendoza, CFE, CIE
Examiner In Charge
State of Washington

Subscribed and sworn to before me this _____ day of _____, 1997.

Colleen Jansen, Notary Public in and
for the State of Washington, Residing in
Seattle, Washington.

